

CITY OF SAN DIEGO  
FISCAL YEAR  
**2008** PROPOSED  
BUDGET

# Fiscal Recovery



# Mayor's Commitment to Fiscal Recovery

In the Fiscal Year 2008 Proposed Budget, the City of San Diego will remain focused on achieving fiscal recovery by implementing the initiatives outlined by the Mayor in the Five-Year Financial Outlook. The Fiscal Year 2008 Proposed Budget funds the eight significant areas that are the legal obligations of the City and have been discussed for years but either never addressed or severely under funded: pension and retiree health obligations; funding of reserves; deferred maintenance and capital improvements; American with Disabilities Act (ADA) improvements; storm water permit compliance; and the Public Liability and Workers' Compensation funds. By establishing a multi-year financial plan, the Mayor has set the framework in the budgeting process for a close examination of City services.



The Fiscal Year 2008 Proposed Budget reaffirms the Mayor's efforts to restore fiscal health to San Diego by continuing commitments to ensure the protection of core services, implementing a managed competition plan, continuing to carry out Business Process Reengineering, and reorganizing the City's operational structure.

## Provision of Core General Fund Services

The City continues to look at various services funded by General Fund to ensure that only core City services are being paid with General Fund revenues. The core City services are:

- Public Safety Services
- Park and Recreation Services
- Transportation Services
- Library Services
- Facility Maintenance Services

The Fiscal Year 2008 Proposed Budget continues to provide the necessary funding for essential services such as police and fire protection, trash collection, and water and wastewater services. However, given the obligations identified in the Five-Year Financial Outlook, the City must concentrate on fulfilling primary core responsibilities at optimum funding levels before committing to other, non-core services.

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## Business Process Reengineering

Through the Business Process Reengineering (BPR) initiative, the Mayor is streamlining the City's business practices and creating efficiencies throughout the City between Fiscal Years 2007 and 2009. The intent is to continue to provide a high level of customer service while reducing the costs of providing these services. While positions have not been targeted for elimination through BPR, a large number of positions have been reduced across several departments. The Fiscal Year 2008 Proposed Budget reflects additional position reductions citywide that will be implemented through BPR efforts. Additional savings will be identified in non-personnel expense costs (supplies and services, IT costs, and fringe benefits) as BPR efforts are finalized.

## Citywide Reorganization

The structure of the City continues to undergo a realignment intended to convert the City into a more manageable and responsive organization. These functional organizational shifts will continue to move the City towards complete fiscal recovery while allowing for better use of resources and transparent accountability. The efforts made in Fiscal Year 2007 and continued as part of the Fiscal Year 2008 Proposed Budget to streamline the City's organizational structure resulted in a net reduction of 671.53 FTEs (full-time equivalent positions) in the Fiscal Year 2008 Proposed Budget, including the reductions related to BPR.

In November 2006, the Mayor presented to the Budget and Finance Committee a Five-Year Financial Outlook that outlined the position reductions needed to achieve fiscal recovery. These reductions have been achieved as outlined in the Outlook; many of these positions are vacant and core City services are not expected to be affected.

## Implementing Managed Competition

In November 2006, voters approved Proposition C, allowing the City to competitively bid for certain jobs alongside external vendors and contractors. The goals of the managed competition program include,



but are not limited to, maximizing the quality of service the City provides to its citizens in a cost effective manner. In addition, it is anticipated that managed competition will reduce the cost of services by having City departments compete with private companies on a level playing field. Managed competition is expected to maximize City resources and serve as a catalyst for positive internal City reforms and savings that will improve the fiscal health of the City.

## Maintaining Sound Financial Structure

In order to achieve a balanced budget, the Mayor's Five-Year Financial Outlook identified significant areas that had been ignored in the past or severely under funded. Adequate funding of these eight areas is essential for the City to achieve fiscal strength and to begin to pay for long overdue capital needs of the City:

- Employee Pension Plan
- General Fund reserves
- Deferred maintenance and capital improvement needs
- Retiree Health (Other Post Employment Benefits)
- Requirements for Storm Water Runoff Permits
- Obligations under the Americans with Disabilities Act
- Workers' Compensation Fund
- Public Liability Fund

## Funding the Pension Plan

Restoring the integrity of the City's Retirement System has been a top priority for the long-term fiscal health and stability of the City. In November 2006, voters approved the passage of Proposition B, the Mayor's initiative calling for voter approval in allowing any future increases in pension benefits for City employees. On June 2006, the San Diego City Employees' Retirement System (SDCERS) released its 2006 actuarial valuation report for the City of San Diego and determined that the City's Annual Required Contribution (ARC) for Fiscal Year 2008 was \$137.7 million.

In Fiscal Year 2008, the City is committed to paying the normal cost and the unfunded liability cost and will contribute \$20 million in addition to the ARC of \$137.7 million. This amount will pay down the Unfunded Actuarial Accrued Liability (UAAL) with no negative amortization. In addition, the City has budgeted an additional \$7.3 million to begin paying back the pension plan for assets spent inappropriately in prior years on retiree health. For Fiscal Year 2008, the City's total pension payment is budgeted at \$165.1 million.

## Building Strong Reserves

The City maintains several reserves for its operations, including the Unappropriated Reserve for the General Fund. The Unappropriated Reserve was established to fund major emergencies such as natural disasters, catastrophic occurrences, excessive liabilities, or judgments. These situations could potentially have a significant impact to the General Fund Unappropriated Reserve. In addition, a healthy reserve assists the City in securing lower interest rates and maintaining a favorable bond rating, saving the City and the taxpayers millions of dollars. A strong reserve also helps insulate the City services against periodic swings in the economy. In October 2002, the City Council adopted a policy providing for the establishment of the General Fund Reserve at a minimum of 3.0 percent of the General Fund revenues. The current policy further defines a goal of a 5.0 percent reserve, to be achieved by 2014. To ensure progress towards this goal, the Council Policy provides that when General Fund revenues increase by at

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least 2.0 percent, there will be a corresponding increase in the General Fund reserve equal to at least 10.0 percent of any General Fund revenue increase in excess of 2.0 percent. It is the goal of the Mayor to go above and beyond this policy and increase reserves to 8.0 percent by Fiscal Year 2012. The Five-Year Financial Outlook established a 6.0 percent reserve goal for Fiscal Year 2008, and the Fiscal Year 2008 Proposed Budget includes \$5.0 million as a contribution to the General Fund Unappropriated Reserve to meet this goal.

## **Funding Deferred Maintenance**

Over the years, the City has undertaken several studies to catalogue deferred maintenance needs for which no funding had been identified. Presently, staff is compiling an inventory of all needs and will have a completed list with the estimated projected costs during Fiscal Year 2008. It is estimated that the City's deferred maintenance and capital needs, excluding Water and Wastewater, may be at least \$800 to \$900 million.

The forecast for addressing the City's deferred maintenance needs in Fiscal Year 2008 assumes that \$5.0 million will be spent on facility repairs and improvements, all of which will be paid in cash. Additionally, \$33 million will be spent in Fiscal Year 2008 to address the deferred maintenance of the City's storm drains and streets. The City's formula for financing storm drain and streets maintenance assumes that 25 percent of costs will be paid in cash while the remaining 75 percent is financed. The Fiscal Year 2008 Proposed Budget includes \$15.7 million in additional funding to accomplish these projects.

## **Addressing Rising Retiree Health Care Costs**

The City continues to experience financial pressure from the rising costs of retiree health care. Under the terms mandated by the Governmental Accounting Standards Board (GASB 45), public agencies across the country, including the City, will be required to report and record this liability on its financial statements. The Fiscal Year 2008 Proposed Budget continues to include funding for these costs on a 'pay-as-you-go' basis, the base cost being \$23.0 million for the fiscal year. The budget also includes an additional \$25.0 million payment for the trust fund to cover the future liability for retiree health driven in part by escalating health care costs.

## **Meeting New Storm Water Runoff Requirements**

Compliance with new Storm Water Runoff regulations associated with new permits has created a large impact on the City's budget. Preliminary estimates show that it will cost the City an additional \$18.0 million in Fiscal Year 2008 to comply with the requirements and this amount has been included in the Fiscal Year 2008 Proposed Budget. The full impact of these regulations on the City's finances in future years is still being analyzed.



## Continuing Compliance with the Americans with Disabilities Act

The Americans with Disabilities Act (ADA) went into effect in 1990, requiring public and private agencies to make facilities and infrastructure universally accessible. Similar to the City's deferred maintenance situation, very little funding has been put toward meeting ADA requirements. ADA improvements are permanent improvements to public sidewalks, facilities and include additional capital projects such as the installation of audible signals at intersections. To

address this important obligation, the Fiscal Year 2008 Proposed Budget includes an additional \$10 million for ADA related improvements. This is in addition to existing Community Development Block Grant funding or other funding allocated for this purpose.



## Building the Workers' Compensation Reserve Fund

Workers' Compensation liabilities continue to grow and sufficient reserves need be put in place by the City to cover increases in these liabilities. The City has approximately \$150 million in outstanding workers' compensation claims and only \$18 million in reserves. This is far short of what should reasonably be expected for the size of the liability; if the City would be required to make a large payout on a claim, there would be a significant impact on General Fund services. By establishing an acceptable reserve level, the City will provide better protection against impacts experienced by General Fund services as a result of these liabilities. The City will begin to fund reserve levels as outlined in the Five-Year Financial Outlook. The Fiscal Year 2008 Proposed Budget includes \$26.1 million to cover only the projected annual costs.

## Building the Public Liability Reserve Fund

Similar to workers' compensation liabilities, the City has public liabilities that fluctuate from year to year and any excessive payouts would create an impact on General Fund services. The City has approximately \$100 million in potential public liability claims and no reserves. The establishment of a sufficient reserve would insulate General Fund services from a detrimental payout if the City were found liable in a claim. The Fiscal Year 2008 Proposed Budget includes \$5.0 million in new funding for a total of \$18 million that includes \$13 million for projected annual costs.

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## Cumulative Budget Impact

The Five-Year Financial Outlook projected that after meeting the funding needs in the eight significant areas and continuing to fund core City services, expenditures would exceed revenues in the General Fund by \$87 million. Corrective actions outlined in the Outlook were implemented in the Fiscal Year 2008 Proposed Budget along with additional savings achieved through streamlining efforts, position reductions and a lower than expected Annual Required Contribution (ARC) to SDCERS.

The projected cumulative budget impact for all City funds in the Five-Year Financial Outlook from the eight significant areas described above totaled \$108.3 million; the projected impact to the General Fund totaled \$94.1 million. The actual impact in the Fiscal Year 2008 Proposed Budget totals \$98.7 million for all City funds and \$70 million for the General Fund. One factor that contributes to the decrease in the projected budget impact is the reduction in the legally required employee pension contribution computed by the San Diego City Employees' Retirement System. The amount budgeted in Fiscal Year 2008 for the City is \$165.1 million for ARC, ARC Plus and the retiree health payback compared to the projected amount of \$198.7 million in the Five-Year Financial Outlook. Also, part of the contributions for the deferred maintenance and the ADA compliance have not changed from the original projections but were budgeted in the Capital Improvements Programs Budget instead of the General Fund.

Table I below demonstrates the comparison between the original projections in the Five-Year Financial Outlook and the amounts included in the Fiscal Year 2008 Proposed Budget.

<b>TABLE I TOTAL CITY CUMULATIVE BUDGET IMPACT FUNDING FOR EIGHT SIGNIFICANT AREAS (In Millions)</b>				
	<b>Five-Year Financial Outlook FY 2008 Projected</b>		<b>FY 2008 Proposed</b>	
	<b>All Funds</b>	<b>General Fund</b>	<b>All Funds</b>	<b>General Fund</b>
ARC Plus <sup>(1)</sup>	\$ 27.0	\$ 20.8	\$ 20.0	\$ 15.0
Reserves <sup>(2)</sup>	7.4	7.4	5.0	5.0
Deferred Maintenance <sup>(3)</sup>	15.7	15.7	15.7	10.4
OPEB	25.0	17.0	25.0	16.6
Storm Water Runoff Compliance	18.2	18.2	18.0	18.0
ADA Compliance <sup>(4)</sup>	10.0	10.0	10.0	-
Workers' Compensation Fund	-	-	-	-
Public Liability Fund	\$ 5.0	\$ 5.0	\$ 5.0	\$ 5.0
<b>TOTAL</b>	<b>\$ 108.3</b>	<b>\$ 94.1</b>	<b>\$ 98.7</b>	<b>\$ 70.0</b>

<sup>(1)</sup> The ARC Plus contribution is less than the original projection due to the updated (lowered) contribution to pay down the Unfunded Accrued Actuarial Liability as computed by the San Diego City Employees' Retirement System actuary.

<sup>(2)</sup> The contribution to the Unappropriated Reserve is lower than the original projection in the Outlook based on the Fiscal Year 2007 year-end projections for the General Fund Reserves.

<sup>(3)</sup> The contribution to the Deferred Maintenance has been budgeted as follows: \$10.4 million in General Fund and the remaining \$5.3 million in the Capital Improvements Program Budget.

<sup>(4)</sup> \$10 million for ADA compliance has been budgeted in the Capital Improvements Program Budget.

The Fiscal Year 2008 Proposed Budget provides funding for the eight significant areas and clearly demonstrates the Mayor's commitment to the implementation of the Five-Year Financial Outlook to restore and maintain the City's sound financial structure.

## **Corrective Actions Incorporated into the Fiscal Year 2008 Proposed Budget**

In order to achieve a balanced budget, several solutions from the Five-Year Financial Outlook have been implemented in the Fiscal Year 2008 Proposed Budget. Table II shows the description of corrective actions between the original projections in the Five-Year Financial Outlook and the estimates included in the Fiscal Year 2008 Proposed Budget.

### **Positions Reductions \$53.5 Million**

A total of 671.53 positions outlined in the Mayor's Five-Year Financial Outlook have been eliminated in the Fiscal Year 2008 Proposed Budget for total salary and benefit savings of \$53.5 million. The total net reduction of 671.53 positions in the Fiscal Year 2008 Proposed Budget includes the reductions related to Business Process Reengineering as well as reductions of middle management and supervisory positions.

The Financial Outlook targeted a total of 671.34 position reductions: 312.80 FTE position reductions in the General Fund and 358.54 positions in the other funds. The Fiscal Year 2008 Proposed Budget reflects a total reduction of 671.53 positions: 296.01 FTE from the General Fund, for a savings of \$20 million, and 375.52 positions from the Non-General Funds for \$33.5 million in savings in Fiscal Year 2008 and future years.

### **Debt Refinancing (PETCO Park) \$3.7 Million**

On January 30, 2007, the City Council adopted the Financing Ordinance authorizing the issuance of lease revenue bonds to refund the previously issued Ballpark Project bonds. The annual debt service on the refunding bonds is \$11.3 million for Fiscal Years 2008 – 2032, which translates into savings of approximately \$3.7 million per year for the General Fund.

### **Reallocation of Transient Occupancy Tax \$15 Million**

The Fiscal Year 2008 Proposed Budget allocates \$15 million or 1.0 cent of the discretionary TOT revenue back to the General Fund and is primarily comprised of the expected savings from the Tourism Marketing District (TMD) (\$7.6 million), the PETCO Park bond refinancing (\$3.7 million) described above, and revenue growth (\$3.7 million).

The San Diego's Lodging Industry Association and the San Diego County Hotel/Motel Association proposed a 2.0 percent assessment on nightly hotel room rentals to TMD with the purpose of creating funding for the marketing of San Diego to potential visitors, which, if approved, would raise approximately \$24.0 million annually. The TMD proposal would offset \$10.0 million annually in funding for organizations that are currently funded by the City for marketing and tourism promotion. The Fiscal Year 2008 Proposed Budget recommends the re-direct of these offset funds back to the General Fund to be used to support other City services, in accordance with Council Policy 100-3, which stipulates that 1.0 cent of 10.5 cents collected from TOT should be allocated for any purposes approved by the Mayor and



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City Council. The Fiscal Year 2008 General Fund Proposed Budget includes estimated \$7.6 million in savings in TOT revenue from the TMD. The TMD proposal is expected to be brought before the City Council by September 2007. An additional \$3.7 million of TOT reallocation is projected growth in the City's TOT revenue.

## **General Government Service Billing \$5.8 Million**

The City's General Fund pays for basic City services such as public safety, parks and libraries. In addition, the City allocates the costs associated with central service departments, such as Auditor and Comptroller, City Attorney, City Clerk and Financial Management to all City departments by means of a rate based on the General Government Services Billing (GGSB) standard. The amounts allocated to Non-General Fund departments are billed and received into the General Fund as revenue to offset the cost of the services provided by these central service departments. In reviewing the allocation of citywide costs, it was determined that the City's General Fund inappropriately supports the total cost of several departments, including the Offices of the Mayor, City Council, the Chief Operating Officer, and similar support services. Based on the GGSB standard, it was determined that the General Fund is currently paying more annually than its appropriate share. Implementing this corrective action results has a net zero effect on the City's total budget; however, the increased revenue to the General Fund provides direct relief to the City's operations funded by taxes. The Fiscal Year 2008 Proposed Budget includes \$5.8 million in revenue from the GGSB.

## **Leveraging City Assets \$15.3 Million**

The Real Estate Assets Department has identified properties for sale that will generate one-time revenue. To comply with the City Charter, revenues generated from the sale of public property will be used for funding of capital projects. The Fiscal Year 2008 Proposed Budget includes \$15.3 million in revenue from the sale of public property which has been budgeted in the Capital Improvements Program Budget to fund ADA and capital improvements for the City-owned facilities.

## **Other Adjustments**

Employee Benefits adjustments are not reflected in the Fiscal Year 2008 Proposed Budget since these modifications are under study and will require discussions with the City's labor unions during Fiscal Year 2008.

The Auditor and Comptroller will release inactive fund balances and aged encumbered funds (projected to be \$2.1 million and \$3.0 million, respectively, in the General Fund). As a result, the General Fund Reserve will have a one-time increase to the fund balance of approximately \$5.1 million.

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<b>TABLE II</b> <b>FISCAL YEAR 2008 PROPOSED BUDGET CORRECTIVE ACTIONS</b> <b>TOTAL CITY</b> <b>(In Millions)</b>		
	FY 2008 Projected	FY 2008 Proposed
Total City Net Reduction of 671.53 FTEs (Five-Year Financial Outlook Projection - 671.34 FTEs)		\$ 53.5
<b>TOTAL REDUCTION</b>		<b>\$ 53.5</b>
<b>FISCAL YEAR 2008 PROPOSED BUDGET CORRECTIVE ACTIONS</b> <b>GENERAL FUND</b> <b>(In Millions)</b>		
	FY 2008 Projected	FY 2008 Proposed
Net Reduction of 296.01 FTEs (312.8 FTEs in Five-Year Financial Outlook)	\$ 25.1	\$ 20.0
Employee Benefit Adjustments/Furlough	4.3	-
Debt Refinancing (PETCO Park)	3.8	3.7
Reallocation of Transient Occupancy Tax	6.0	11.3
Budget Clean-up		
Corrected GGSB (General Government Services Billing)	3.2	5.8
Inactive Fund Balances	2.1	2.1
Release of Encumbered Funds	3.0	3.0
Leveraging City Assets	15.3	15.3
Managed Competition	tbd	tbd
<b>TOTAL CORRECTIVE ACTIONS</b>	<b>\$ 62.8</b>	<b>\$ 61.2</b>

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## **Service Level Impacts**

A net total of 671.53 positions citywide have been eliminated in the Fiscal Year 2008 Proposed Budget, one of the key corrective actions outlined in the Mayor's Five-Year Financial Outlook. A reduction in service levels is not anticipated since the majority of these positions were vacant for a significant period of time or were eliminated as a result of Business Process Reengineering.

A portion of the 671.53 positions that are being eliminated are also the result of the reduction in expenditures that General Fund departments were requested to make to help balance the budget in Fiscal Year 2008. General Fund departments identified solutions to fund the projected gap of approximately \$25 million between projected General Fund expenditures and revenues. Departments proposed expenditure reduction plans of either 4.0 percent or 10 percent, depending on whether the department had completed BPR (4.0 percent for departments having completed BPR and 10 percent for departments that had not begun BPR). As a result of this process, 22.00 of the 671.53 FTE positions were eliminated. The full effect of all position reductions are difficult to gauge at this time, although no program closures have been identified as possible outcomes.

## **Funding of Positions for New Facilities**

The Five-Year Financial Outlook included funding for several new facilities and the annualization of budgeted staff for existing facilities. These facilities were funded in the Fiscal Year 2008 Proposed Budget with the exception of 15.50 sworn positions for the Northwestern Area Station. The new funding for the Northwest station in Fiscal Year 2008 includes 4.50 FTE civilian positions and approximately \$1.2 million in non-personnel support.

The Fiscal Year 2008 Proposed Budget achieves the goal of the City's comprehensive Five-Year Financial Outlook. It addresses and provides funding for many areas that have been either ignored or under funded in the past. The City's adherence to its Five-Year Financial Outlook demonstrates continued commitment to build a solid fiscal foundation for the provision of core services to the citizens of San Diego